

employee plans news

PROTECTING RETIREMENT BENEFITS THROUGH EDUCATING CUSTOMERS

Internal Revenue Service
Tax Exempt and Government
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A Publication of Employee Plans

Have We Got a Proposal For You: 403(b) Proposed Regulations

On November 15, 2004, a momentous event occurred in the world of 403(b) tax-sheltered annuities. The first [comprehensive regulations](#) in 40 years were issued. These regulations were released in proposed form and state that they cannot be relied upon until finalized. They reach out beyond 403(b) to provide guidance on 402(b), 402(g), 414(c), and 3121(a)(5)(D). There is a general effective date, when finalized, which will be for taxable years beginning after December 31, 2005, with some notable exceptions. The [3121\(a\)\(5\)\(D\) companion piece](#) is a temporary regulation and is effective on the November 16, 2004 date of publication, and the portion dealing with the grandfathering of incidental life insurance contracts applies to contracts issued up to 90 days from the publication date. Churches sponsoring 403(b)s and collectively bargained situations may experience a later effective date.

ACT Now

The IRS is seeking applications for two EP vacancies on the Advisory Committee on Tax Exempt and Government Entities (ACT). The committee provides a venue for public input into critical tax administration areas. Applications can be made by letter or by completing an [application form](#). A [notice](#) published in the Federal Register, Nov. 1, 2004, contains more details. •

So what does proposed mean? It means nothing, it means everything. The IRS cannot conduct any examination enforcement activity based on them. However, it is necessary not only to be aware of what may be coming but also what it will take to live under them when they are finalized. So that you may participate in helping to shape their ultimate form, there is a public comment period and a public hearing scheduled for February 15, 2005.

So let's explore the highlights of the proposed regulations including what existing IRS positions have been acknowledged, what is brand new and what guidance is yet to come.

The proposed regulations cover 403(b)s that provide for vesting, as well as overall general disaggregation with 401(a) defined contribution plans. The fact that the 414(v) age 50 catch up comes only after the application of 402(g)(1) and 402(g)(7) dollar limitations is discussed. The nonelective nature of post-severance contributions (up to 5 years) is acknowledged. Meaningful notice needed to satisfy the universal availability for salary reduction contributions and the fact that hardship distributions follow the 401(k) rules are included. Finally, the 3121(a)(5)(D) Temporary Regulation makes it clear that employment taxes apply to condition of employment salary reduction 403(b)s even though they are not cash or deferred elections.

And now, for the brand new highlights, foremost of which is that the proposed regulations require that a 403(b) program be maintained pursuant to a written defined contribution plan which in both form and operation satisfies 403(b) and contains all the terms and conditions for benefits under the plan. The proposed regulations provide that 403(b) elective deferrals for 403(b) and 402(g) purposes are limited to contributions under a cash or deferred election as defined under 401(k). In addition, organizations with 414(d) and 501(c)(3) status may cover all of their employees under the 403(b). Also, the good faith reasonable standard of Notice 89-23 for nonelective nondiscrimination is not maintained. Of notable interest is that amounts not subject to 403(b)(7) and 403(b)(11) distribution restrictions may be distributed only after severance of employment or upon the occurrence of an event such as after a fixed number of years, the attainment of a stated age under the plan or disability.

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The proposed regulations go on to provide that contribution amounts must be transferred to providers within a period no longer than is reasonable for proper plan administration, such as transferring elective deferrals within 15 business days following the month in which these amounts would have been paid to the participant. They go on to provide that unless grandfathered, incidental insurance may not be part of a 403(b) plan. The proposed regulations provide that these plans may terminate and distribute assets with full rollover ability, as well as recognize the occurrence of an employment severance where an employee no longer works for an employer eligible to maintain a 403(b).

It is intended that Revenue Ruling 90-24, in-service plan-to-plan 403(b) asset transfers, be limited to situations where the employee is a participant of the receiving plan. Finally, church 403(b)(9) retirement income accounts will be expected to be maintained pursuant to a plan which affirmatively states the intent to be a retirement income account.

The 414(c) portion of the proposed regulations addresses aggregation to determine the employer for control group benefit purposes for all exempt organizations, except churches, based upon an 80% director or trustee common control test.

Finally, we are told in the proposed regulations to expect future guidance on post-severance deferrals for 403(b)s, 457(b)s and 401(k)s to be located in the upcoming 415 regulations, and to expect an update of Revenue Ruling 2004-67 to include 403(b)(7) custodial account assets as well as assets of 403(b)(9) retirement income accounts to be included in 81-100 trusts.

So, welcome to what may well be a brave new world for 403(b). •

A Determination Letter Program for 403(b) Plans?

(Editor's note: With the long-anticipated issuance of guidance on 403(b) plans now a reality, Carol Gold, Director of EP, wanted to address a related topic that has received some public interest: Will EP establish a DL program for 403(b) plans? Ms. Gold has prepared some comments below on this subject.)

EP has been considering the future possibility of a determination letter program—but we're not quite ready to implement one yet. We are also currently in the throes of establishing a new determination letter program structure that we want to get up and running smoothly before attempting to address a determination letter program for 403(b) plans. However, I did want to sketch out where we are on 403(b) plans in general.

This week, proposed regulations under section 403(b) were published in the Federal Register. These regulations take the important step of requiring a 403(b) contract to be maintained pursuant to a plan in order for amounts contributed by employers for the purchase of annuity contracts to be excluded from the gross income of employees. For purposes of the regulation, a plan is a written defined contribution plan which must satisfy the applicable requirements of the regulation both in form and operation. Furthermore, the proposed regulation provides rules by which 403(b) plans may be terminated.

Clearly, the proposed regulations move the "403(b) plan" closer to the concept of a "qualified plan". However, we anticipate it will be a while yet before the regulations are finalized. Nevertheless, we recognize that if 403(b) annuity contracts are treated as "plans" under the regulations when finalized, there will be more of an impetus to create a program to review plans and plan amendments, and possibly to issue determination letters on those plans or amendments.

We would welcome the opportunity to work with the public on considering such a program. At this point, however, we feel it would be premature to actively develop such a program prior to the finalization of the regulation. Therefore, I would suggest that we continue to exchange ideas about what a program could look like while agreeing that substantive change will have to wait a little longer.

If you have comments or suggestions, please contact us at RetirementPlanComments@irs.gov. •

New Publication Now Available Online

By popular demand, we've created a new brochure, **Publication 4406, 403(b) and 457 Retirement Plans (with Plan Feature Comparison Chart)**. This new product makes use of an easy-to-read chart that outlines the key features of 403(b) and 457 plans while comparing them to 401(k) plans. The publication is available on the [Retirement Plans web page](#) by clicking on "EP Forms & Publications" under the "Related Topics" section and will be available in hardcopy sometime after December 1st by calling 1-800-TAX-FORM. •

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